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D. Michael Case

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BREACH OF WARRANTY—RIGHTS AND OBLIGATIONS

D. MICHAEL CASE*

THIS ARTICLE examines the breach of warranty endorsement of an aircraft insurance policy and the respective rights and obligations of the parties to the policy, focusing on the most troublesome subjects and the most frequently arising controversies. For purposes of this study, "BOW" refers to the breach of warranty or lienholder's single interest endorsement, because the terms are generally used synonymously.¹ The elements of the BOW itself must be explored, however, before the rights and obligations of the parties are examined.

Generally two types of insurance clauses are used to protect the interest of the mortgagee: (1) the "loss payable" or "ordinary mortgage clause"; and (2) the "standard" or "union mortgage clause". A mortgagee claiming under a loss payable clause or ordinary mortgage clause is nothing more than an assignee, and his rights are subject to all defenses that the insurer may have against the mortgagor.² The standard mortgage clause or union mortgage clause, on the other hand, provides that the mortgagee is protected against a loss resulting

* Corporate Counsel, Cessna Finance Corporation. B.A., 1966, Southwestern College; J.D., 1972, Washburn University of Topeka. Mr. Case is a member of the Kansas Bar, the current President of the Aircraft Finance Association, and 1980 President of the Wichita Corporate Counsel Society.

¹ Some state insurance commissioners, for example, those in Kansas, have determined that there is no breach of warranty endorsement, and consequently it is termed a lienholder's single interest endorsement.

² ANDERSON, COUCH ON INSURANCE § 42:671 (1962) [hereinafter cited as ANDERSON]; 5A APPLEMAN, INSURANCE LAW AND PRACTICE § 3402 (1970) [hereinafter cited as APPLEMAN].

from any act or neglect by the mortgagor and that an act or neglect by the mortgagor shall not defeat the insurance coverage as to the mortgagee.³

The BOW attached to an aircraft insurance policy is traditionally a standard mortgage clause and has been patterned after the New York Standard Mortgage Clause.⁴ The New York Standard Mortgage Clause was developed and used in

³ ANDERSON, *supra* note 2, § 42:682-719; APPLEMAN, *supra* note 2, § 4164.

⁴ See N.Y. INS. LAW § 168 (McKinney 1966). The New York Standard Mortgage Clause states:

loss, if any, under this policy, shall be payable to the aforesaid as mortgagee (or trustee) as interests may appear under all present or future mortgages upon the property herein described in which the aforesaid may have an interest as mortgagee (or trustee), in order of precedence of said mortgages, and this insurance, as to the interests of the mortgagee (or trustee) only therein, shall not be invalidated by any act or neglect of the mortgagor or owner of the within described policy, nor by any foreclosure or other proceedings or notice of sale relating to the property, nor by any change in the title or ownership of the property, nor by the occupation of the premises for purposes more hazardous than are permitted by this policy; provided, that in case the mortgagor or owner shall neglect to pay any premium due under this policy, the mortgagee (or trustee) shall, on demand, pay the same.

Provided, also, that the mortgagee (or trustee) shall notify this company of any change of ownership or occupancy or increase of hazard which shall come to the knowledge of said mortgagee (or trustee) and, unless permitted by this policy, it shall be noted thereon and the mortgagee (or trustee) shall, on demand, pay the premium for such increased hazard for the term of the use thereof; otherwise this policy shall be null and void.

This company reserves the right to cancel this policy at any time as provided by its terms, but in such case this policy shall continue in force for the benefit only of the mortgagee (or trustee) for ten days after notice to the mortgagee (or trustee) of such cancellation and shall then cease, and this company shall have the right, on like notice, to cancel this agreement.

Whenever this company shall pay the mortgagee (or trustee) any sum for loss under this policy and shall claim that, as to the mortgagor or owner, no liability therefore existed, this company shall, to the extent of such payment, be thereupon legally subrogated to all the rights of the party to whom such payment shall be made, under all securities held as collateral to the mortgage debt, or may, at its option, pay to the mortgagee (or trustee) the whole principal due or to grow due on the mortgage with interest, and shall thereupon receive a full assignment and transfer of the mortgage and of all such other security; but no subrogation shall impair the right of the mortgagee (or trustee) to recover the full amount of said mortgagee's (or trustee's) claim.

Id.

connection with fire insurance policies for real estate. Unlike real estate, aircraft are highly mobile, and aircraft and pilots must be certified or licensed under applicable provisions of the Federal Aviation Act of 1958.⁵ Therefore, the standard mortgage clause has been modified for aircraft and, although specific clauses vary, a typical clause provides:

This endorsement extends your coverage under part 2—Aircraft Physical Damage—to protect the interests of the lienholder shown below, even if coverage is otherwise invalidated by any act or neglect.

1. Aircraft Description, lienholder and loan balance. [Identification of aircraft].

2. Adjustment in Payment.

Aircraft physical damage under Coverage F or G will be adjusted with you and payment will be made to you and the lienholder shown above for the damaged aircraft.

3. Payment to lienholder only.

We will pay the valid claim of the lienholder of the aircraft shown in Paragraph 1 above if: (a) there would otherwise be coverage for the claim except for any act or neglect resulting in our denial of payment to you; and (b) the lienholder (1) has notified us of any change in ownership or substantial change in risk of which the lienholder was aware; (2) pays any premium due under this policy on demand if you have neglected to pay the premium; and (3) gives us a sworn proof of loss within 90 days after receiving notice from us of your failure to do so.

4. What we will pay.

Under paragraph 3 above, we will pay the lienholder the lesser of the following: (a) the unpaid balance of the lien on the aircraft, less unearned interest and unpaid installments more than 30 days overdue on the date of the loss or damage; or (b) the amount shown under "loan balance" in Paragraph 1 above; or (c) 90% of the agreed value of the aircraft.

5. When we will pay.

Under paragraph 3 above, we will pay the lienholder within 30 days after: (a) the lienholder has used all reasonable means to collect the amounts due from you; and (b) you have given us a sworn proof of loss statement or the lienholder has done so

⁵ 49 U.S.C. § 1422-1423 (1981).

within 90 days after receiving notice from us of your failure to do so.

6. Our right of recovery.

If we pay the lienholder for any claim and deny payment to you because of any act or neglect that invalidates your coverage: (a) we will take over the rights granted under the promissory note, mortgage, lien or contract to the lienholder against you and in and to all the property held as security for the loan to the extent of our payment; or at our option, we may pay the lienholder the whole amount due or to become due from you with interest and take a full assignment and transfer of all of the rights of the lienholder against you and of all property held as security for the loan; and (b) you must pay us back in full for the payment we make.

7. What we will not pay.

We will not pay any claim by anyone if you or anyone you permit to fly your aircraft embezzles, converts or secretes the aircraft or if there has been a change in title or ownership.

8. Legal action against us.

No legal action shall be brought against us under this endorsement until its provisions have been complied with fully.

9. Cancellation notice to lienholder.

If we cancel your aircraft physical damage coverage, we will send 30 days prior written notice to the lienholder at the address shown in this endorsement.*

Three separate entities, each assuming several roles, are affected by the BOW. For simplicity, throughout this paper the named insured, mortgagor or borrower will be referred to as the "mortgagor." The creditor, lender, or mortgagee will be referred to as the "mortgagee," and the insurance company will be referred to as the "insurer". In all instances the aircraft insurance policy containing a BOW creates a three-party relationship between the insurer, mortgagor and mortgagee. The law is well settled throughout the country that the BOW creates and constitutes a separate insurance policy between

* Lienholders interest endorsement, Aviation Office of America (Form No. 2235-79). Plain English—The Plain English form is presented because many states now require that policies of insurance be written in that form. *Standard Fire Policies, FIRE & CASUALTY CAS. (CCH) ¶ 2001-2106 (1982).*

the lienholder and the insurer.⁷

The important feature of the BOW is that the underlying policy terms are not nullified, but a new and separate contract is made between the insurer and the mortgagee.⁸ Neither the mortgagor's contract nor the mortgagor's acts bind the mortgagee. Therefore, the mortgagee is not in the precarious position of having his coverage destroyed by the ignorance, carelessness or negligence of the mortgagor.

Because the BOW is a separate contract of insurance, an additional premium may be charged for the coverage. The payment of an additional premium illustrates that the BOW's affect on the mortgagee's status is substantially greater than simply making him an additional named insured under a loss payable clause. This is further illustrated by the fact that the mortgagor and mortgagee are kept separate throughout the BOW.⁹

The BOW is almost always written in a stated or agreed value basis rather than on an actual cash value basis.¹⁰ The recovery of the mortgagee is typically limited to eighty or

⁷ *Piedmont Fire Ins. Co. of Ala. v. Fidelity Mortgage Co.*, 250 Ala. 609, 35 So. 2d 352 (1948); *American Mercury Ins. Co. v. Inland-Western Fin. Co.*, 6 Ariz. App. 409, 433 P.2d 60 (1967); *National Casualty Funding Corp. v. Motors Ins. Corp.*, 59 Cal. 2d 91, 387 P.2d 361, 28 Cal. Rptr. 161 (1963); *Glenn Falls Ins. Co. v. Porter*, 44 Fla. 568, 33 So. 473 (1902); *Security Ins. Co. v. Commercial Credit Equip.*, 399 So. 2d 31 (Fla. Dist. Ct. App. 1981); *AirVac, Inc. v. Ranger Ins. Co.*, 266 So. 178 (Fla. Dist. Ct. App. 1972); *Aetna Life & Casualty Co. v. Charles S. Martin Distrib. Co.*, 120 Ga. App. 133, 169 S.E.2d 695 (1969); *Fred v. Pacific Indem. Co.*, 53 Hawaii 384, 494 P.2d 783 (1972); *Guardian Sav. & Loan Ass'n v. Ranger Ins. Co.*, 2 Ill. App. 3d 77, 267 N.E.2d 109 (1971); *Cessna Fin. Corp. v. Ranger Ins. Co.*, 15 Av. Cas. 17,309 (D. Kan. 1979); *Hartford Fire Ins. Co. v. Associates Capital Corp.*, 313 So. 2d 404 (Miss. 1975); *AVEMCO Ins. Co. v. Jefferson Bank & Trust Co.*, 16 Av. Cas. 17,242 (Mo. Ct. App. 1980); *National Factors, Inc. v. Waters*, 42 Misc. 2d 822, 249 N.Y.S.2d 121 (Sup. Ct. 1964); *Western Leasing, Inc. v. Occidental Fire & Cas. Co. of N.C.*, 268 Or. 426, 521 P.2d 352 (1974); *Osborne v. Pacific Ins. Co. of N.Y.*, 91 R.I. 469, 165 A.2d 725 (1960); *St. Paul Fire & Marine Ins. Co. v. Kretschfield*, 163 Tex. 586, 350 S.W.2d 534 (1961); *Bennett Motor Co. v. Lyon*, 14 Utah 2d 161, 380 P.2d 69 (1963). *ANDERSON, supra* note 2, § 42:694; *Appleman, supra* note 2, § 3401.

⁸ *ANDERSON, supra* note 2 § 42:671; *Appleman, supra* note 2, § 3402.

⁹ *Standard Fire Policies, FIRE & CASUALTY CAS. (CCH) ¶ 2001-2106* (1982).

¹⁰ See *supra* note 6 and accompanying text. See also *United States Aviation Underwriters, Inc.* (Form 369-AZ REV 10-79); *Southeastern Aviation Underwriters, Inc.* AV-19 (1-80); *Associated American Underwriters, Inc.* (Form AAU-4: London Form AV-28); *AVEMCO Insurance Company Form ERPE 3* (1-81); and *National Aviation Underwriters Form PLL 749* (12-80).

ninety per cent of the agreed value of the aircraft or the loan balance remaining, less unpaid installments past due thirty days or more, whichever is less.¹¹

The BOW imposes several particular obligations on the mortgagee. The mortgagee is required to pay premiums if the mortgagor fails to pay them,¹² and the mortgagee must notify the insurer of any known increase in hazard or change in title or ownership.¹³ The mortgagee is charged with the responsibility to render proof of loss if the mortgagor fails to do so,¹⁴ and upon payment, to assign to the insurer all rights under the underlying promissory note or security agreement to the extent of such payment.¹⁵ All of these obligations create unique problems which will be discussed later in this article.

When considering some of the specific problem areas of the aircraft BOW, one major caveat should never be forgotten: there are as many BOW forms as there are aviation managers and insurance companies,¹⁶ therefore the particular policy involved must always be examined in great detail. While there are striking similarities in the various policy forms, they are by no means identical, as the following chart indicates:

¹¹ See forms listed in notes 6 and 10 *supra*.

¹² See *id.*

¹³ See *id.*

¹⁴ See *id.*

¹⁵ See *id.*

¹⁶ See, e.g., Avemco Insurance Company, National Aviation Underwriters, Inc., Aero Coverages, Inc., Aero Space Managers, Inc., American Aviation Underwriters, American National General Agencies, Associated Aviation Underwriters, Aviation Office of America, Inc., Bristol Aviation, C.T.H. Aviation Underwriters, Crump Aviation Underwriters, Eastern Aviation/Marine Underwriters, Insurance Company of North America, Pacific Aviation Managers, Southern Marine/Aviation Underwriters, Inc., Southeastern Aviation Underwriters, Inc., Universal Aviation Underwriters, and United States Aircraft Insurance Group, to name but a few.

A COMPARATIVE ANALYSIS OF BREACH OF WARRANTY ENDORSEMENTS¹⁷

INSURER / POLICY	Is Loss Payable Included?	Must Lienholder Advise if Title/Ownership Changes?	Must Lienholder Advise of Increased Hazard & Pay Additional Premium?	Must Lienholder Submit Proof of Loss in 60 Days After Insured Fails To?	Must Lienholder Pay the Premium if Insured Doesn't?	Must Lienholder Use All Reasonable Means to Collect Note From Insured?	Do Deductibles Apply to a B.O.W. Payment?	Must Insurer Advise the Lienholder if Policy is Cancelled by Insured?	Is Embezzlement or Secretion by Persons Other than the Insured in Possession of the Aircraft Covered?
ASSOCIATED GOLDEN WING	YES	YES	YES	YES	YES	YES	NM	NO	YES
AEROSPACE AV. UWRTRS.	YES	YES	YES	YES	YES	YES	NM	NO	AMBIG
AMERICAN AV. UWRTRS.	YES	YES	YES	NM	YES	YES	NM	YES	NM
AOA AIR PLAIN	YES	YES	YES	YES 90D	YES	YES	NM	NO	NO
C.T.H. UNDERWRITERS	NC	NC	YES	YES	YES	YES	NM	NO	NO
CRUMP MONARCH INS CO.	YES	NC	YES	YES	YES	YES	NM	NO	NO
EASTERN AV. UWRTRS.	YES	YES	YES	YES	YES	YES	NM	NO	YES
GLOBAL AV. UWRTRS.	NC	NC	YES	YES	YES	YES	NM	NO	NO
I.N.A. AERO PAC	YES	YES	YES	NM	YES	YES	NM	NO	YES
LLOYD'S, LONDON AV28	NC	YES	YES	YES	YES	YES	NM	NO	YES
SOUTHEASTERN AV. UWR.	YES	YES	YES	NM	YES	YES	NM	NO	YES
SOUTHERN MARINE & AV.	YES	NC	YES	YES	YES	YES	NM	NO	YES
U.S.A.I.G. 360 POLICY	YES	YES	YES	YES	YES	YES	NM	NO	YES
U.S.A.I.G. ALL CLEAR	YES	NO	NO	YES	YES	YES	NM	NO	YES

NM = NOT MENTIONED

NC = CHANGE OF TITLE OR OWNERSHIP NOT COVERED

¹⁷ D. McKensie, *A Comparative Analysis of Breach of Warranty*, (unpublished manuscript) (printed with permission of author). While the chart is several years old and some of the policy forms have been changed, it still illustrates that there are differences in the BOW policy forms.

Some of the policy forms are affected by a "change in title or ownership" while others are not; most, but not all, require the mortgagee to notify the insurer of an increase in hazard; all require the insurer to advise the mortgagee if the policy is cancelled by the insurer; all of the various policy forms are silent as to whether the insurer is responsible for advising the mortgagee in the event the mortgagor cancels the policy; and all the policy forms provide exclusionary language for a conversion, embezzlement or secretion by the named insured, although many are silent as to what happens if persons other than the named insured convert, embezzle or secrete the aircraft.

It goes without saying that, where there is no conflict between the BOW and the main policy terms, conditions and exclusions, coverage issues can be resolved rather easily. For instance, assume the mortgagor is a Visual Flight Rules (VFR) pilot, yet he takes off in Instrument Flight Rules (IFR) conditions. A crash ensues and the aircraft is totally destroyed. Further assume salvage is readily available and the mortgagee is able to peacefully repossess the salvage, as well as provide to the insurer a full assignment of his underlying loan and security documents. In such circumstances, the insurer may deny coverage under the mortgagor's policy, based upon pilot qualifications, while at the same time the insurer may accept coverage under the BOW.

Not all BOW losses are as simple as the hypothetical situation described. Additional factors that cloud the situation include: (1) fraud in the procurement of the mortgagor's policy; (2) damage to the aircraft outside the territorial limits of the main policy; (3) confiscation of the aircraft; (4) disappearance of the aircraft; (5) failure of the mortgagee to gain peaceful possession of the aircraft; or (6) partial loss of the aircraft only. When the additional factors are present, the insurer will argue that the BOW is a "following form" policy, requiring consideration of the underlying terms and conditions of the main policy in determining coverage under the BOW. At the same time, the mortgagee is likely to contend that the BOW is a separate policy, providing coverage in all instances where

the mortgagor breaches his obligations. The mortgagee will allege further that the only exclusions from coverage are for conversion, embezzlement or secretion of the property. These exclusions are found in virtually all policy forms, but with some distinctions as to whether the exclusions apply only to the mortgagor or to one in lawful possession of the aircraft.

FRAUD AND MISREPRESENTATION

Because the BOW is a separate contract and provides that the mortgagee's interest shall not be invalidated by any act or neglect of the mortgagor, the mortgagee's coverage is, as a general rule, unaffected by a false statement made by the mortgagor that could render the mortgagor's insurance void ab initio.¹⁸ Thus, the mortgagee's coverage will not be invalidated by the mortgagor's misrepresentations concerning use of the aircraft, pilot certification, and ownership of the aircraft, even though the policy is void as to the mortgagor.

Coverage under the BOW should also be valid as to the mortgagee, even though the mortgagor did not have an insurable interest in the aircraft. Application of the decision in a Florida case, *AirVac v. Ranger Insurance Co.*,¹⁹ would invalidate a mortgagee's coverage if the mortgagor lacked an insurable interest. The *AirVac* court relied in part on *Western Assurance Co. v. Hughes*,²⁰ a 1937 Oklahoma decision. Unfortunately, the Florida court that decided *AirVac* neglected more recent Oklahoma decisions, such as *Great American Insurance Co. v. Southwestern Financial Co.*²¹ and *Oklahoma State Union v. Folsom*²² in which the Oklahoma

¹⁸ *Syndicate Ins. Co. v. Bohn*, 65 F. 165 (8th Cir. 1894); *AirVac, Inc. v. Ranger Ins. Co.*, 266 So. 2d 178 (Fla. Dist. Ct. App. 1972); *Vormelker v. Oleksinski*, 199 N.W.2d 287 (Mich. Ct. App. 1972); *Bacot v. Phenix Ins. Co.*, 96 Miss. 223, 50 So. 729 (1909); *Oklahoma State Union v. Folsom*, 325 P.2d 1053 (Okla. 1958); *Great Am. Ins. Co. v. Southwestern Fin. Co.*, 297 P.2d 403 (1956); *Western Assurance Co. v. Hughes*, 179 Okla. 1254, 66 P.2d 1056 (1937); *National Fire Ins. Co. v. Dallas Joint Stock Land Bank*, 174 Okla. 1596, 50 P.2d 326 (1935); *Old Colony Coop. Bank v. Nationwide Mut. Fire Ins. Co.*, 332 A.2d 434 (R.I. 1975). See ANDERSON, *supra* note 2, § 42:704.

¹⁹ 266 So. 2d 178 (Fla. Dist. Ct. App. 1972).

²⁰ 179 Okla. 1254, 66 P.2d 1056 (1937).

²¹ 297 P.2d 403 (Okla. 1956).

²² 325 P.2d 1053 (Okla. 1958).

Supreme Court rejected the insurable interest argument and relied solely upon the fact that the BOW was an independent contract.²³ The importance of the insurable interest argument in *AirVac*, however, must not be discounted because the independent contract concept is cogently explained. The Florida court states that the BOW is:

a clause which creates a new contract, creating a relationship of insurer and insured between the insurer and lienholder, so that the policy is not subject to forfeiture because of any act or omission of the mortgagor, whether before or after the issuance of the policy.²⁴

Although the fraudulent acts of the mortgagor may not invalidate coverage as to the mortgagee under the BOW, the mortgagee is protected only if he acts in good faith and does not participate in the fraud or misrepresentation.²⁵ Consistent with such an approach, in *Citizens State Bank v. American Fire & Casualty Co.*²⁶ and *Weekly v. Missouri Property Insurance Placement*,²⁷ the courts held against a mortgagee under a BOW, when the mortgagee became aware of the mortgagor's misrepresentation and failed to notify the insurer.

CONVERSION, EMBEZZLEMENT OR SECRETION

Without exception, if the mortgagee converts, embezzles or secretes the mortgaged property, coverage under the BOW is specifically excluded.²⁸ Whether these same acts by someone who is lawfully in possession, other than the mortgagee, exclude coverage under the BOW, depends upon the specific policy form involved.²⁹ The key issue regarding coverage as to the mortgagee under the BOW, however, may be: what constitutes an act of conversion, embezzlement or secretion?

²³ 325 P.2d at 1056; *Great American Ins. Co. v. Southwestern Fin. Co.*, 297 P.2d at 404.

²⁴ 266 So. 2d at 179.

²⁵ *Id.* at 180-81.

²⁶ 198 F.2d 57 (5th Cir. 1952).

²⁷ 538 S.W.2d 375 (Mo. Ct. App. 1976).

²⁸ See *supra* note 3 and accompanying text.

²⁹ See *supra* text accompanying note 17.

In *Commerce Union Bank v. Midland National Insurance Co.*,³⁰ for example, an action was brought by the mortgagee for a loss sustained as a result of a fire. The insurer denied coverage on the ground that the fire was deliberately set by the mortgagor and therefore a "conversion" caused the loss.³¹ The court agreed with the insurer that the intentional destruction of the property by the mortgagor amounted to a conversion, and therefore coverage was denied.³²

In *National Casualty Co. v. General Motors Acceptance Corp.*,³³ the mortgagor brought an action under a BOW for the loss of an automobile resulting from the mortgagor intentionally running the automobile off a bridge and into a bay. The insurer argued that the mortgagor, in intentionally running the automobile off the bridge, had converted the mortgagee's interest and therefore was excluded from coverage.³⁴ The court described the insurer's argument as "novel," but rejected it, holding that the insurer, by using the word "conversion" in connection with the words "embezzlement and secretion" in the BOW, referred to conversion in the criminal sense rather than as a tort.³⁵ The court reasoned that the owner's intent in destroying the automobile was to cover up his own disappearance by creating the impression that he had an accident, and not to convert the mortgagee's interest. As a result, there was no conversion by the mortgagor within the meaning of the policy exclusion.³⁶

*National Casualty*³⁷ illustrates that "conversion" is *not* defined by the policy and is subject to differing interpretations. Consequently, the interpretation most favorable to recovery should be utilized. *National Casualty*, therefore, is more persuasive authority than the *Commerce Union Bank* case.

³⁰ 43 Ill. App. 2d 332, 193 N.E.2d 230 (1963).

³¹ 193 N.E.2d at 231.

³² *Id.* at 232.

³³ 161 So. 2d 848 (Fla. Dist. Ct. App. 1964).

³⁴ *Id.* at 852.

³⁵ *Id.*

³⁶ *Id.*

³⁷ 161 So. 2d 848 (Fla. Dist. Ct. App. 1964).

REPOSSESSION

Frequently, as a precondition to payment under the BOW, the insurer requires the mortgagee to repossess a damaged aircraft, and furnish a repossession certificate and bill of sale. This prerequisite is based upon the policy conditions regarding assistance and cooperation in subrogation, and the language in the BOW which provides that upon payment the insurer is entitled to "an assignment and transfer of all the rights . . . in and to the property." As previously discussed, however, the BOW is recognized as a separate policy between the insurer and the mortgagee, with its terms controlling the respective rights of the parties.³⁸ The BOW does not require the mortgagee to repossess; it only requires the mortgagee to transfer his interests in the property.³⁹ Transferring an interest in property does not require the transferor to have possession of the property at the time of transfer. Therefore, the attempt by the insurer to require repossession as a prerequisite to payment under the BOW will be ineffective.

Another question arising from the BOW is whether coverage terminates or continues upon the mortgagee's repossession. In *Fayette Bank & Trust v. Ranger Insurance Co.*,⁴⁰ the court held that coverage remained intact and that a loss occurring during the repossession was covered because the repossession itself did not constitute a change in title or ownership in the aircraft.⁴¹ The coverage continued although the aircraft was flown under a ferry permit when the airworthiness certificate had expired, a situation that would have voided the mortgagor's coverage.⁴² The court's decision is questionable though, considering the fact that acts which could have voided coverage were committed by the mortgagee or its agent, not the mortgagor. Consequently, it is arguable

³⁸ See *supra* note 7 and accompanying text.

³⁹ *Cessna Fin. Corp. v. Ranger Ins. Co.*, 15 Av. Cas. 17,309 (D. Kan. 1979); *National Community Bank of N.J. v. Aviation Office of Am., Inc.*, No. 349609, slip op. (N.J. Bergen County Dist. Ct.) (order granting plaintiff's motion for summary judgment).

⁴⁰ 12 Av. Cas. 17,887 (Pa. Commw. Ct. 1972).

⁴¹ *Id.* at 17,888-89.

⁴² *Id.* at 17,889.

that the court should have found no coverage, despite the fact that under the main policy and the BOW, coverage was not automatically terminated upon repossession of the aircraft.

PREMIUM PAYMENT BY MORTGAGEE

Most BOW policy forms provide that "in case the lessee, mortgagor or owner shall neglect to pay any premium due under such policy, the lienholder shall, on demand, pay the same." The key question regarding this language is whether the mortgagee's obligation to pay the premium is a "covenant" or a "condition." If the obligation is a covenant, the mortgagee has an absolute obligation to pay the premium. If the obligation is a condition, the mortgagee need only pay the premium to continue coverage. Most courts have held that the requirement that the mortgagee pay premiums is a condition and have required the mortgagee to pay the premium only if the mortgagee desires to keep the insurance in force.⁴³ The minority rule holds that the mortgagee's obligation to pay past-due premiums is a covenant.⁴⁴

Another question regarding premium payment involves the rather common situation in which the insurance agent advances or finances the premium payment for the mortgagor. In this situation, not only must the insurance agent overcome the majority rule, he must also overcome the additional problem of being a mere volunteer. In either instance, he is not entitled to recover premiums which have been advanced.⁴⁵

Policy forms have differing language regarding the mortga-

⁴³ See, e.g., *Lupke-Rice Ass'n v. Cessna Fin. Corp.*, S76-628, slip op. (Ind. Allen County Super. Ct. Sept. 26, 1979) (order granting defendant's motion for summary judgment); *General Credit Corp. v. Imperial Casualty & Indem.*, 167 Neb. 833, 95 N.W.2d 145 (1959); *Whitehead v. Wilson Knitting Mills*, 194 N.C. 281, 139 S.E. 456 (1927); *Johnson, Sansom & Co. v. Fort Worth State Bank*, 244 S.W. 657 (Tex. Civ. App. — El Paso 1922, no writ).

⁴⁴ *Stoddart v. Black*, 134 Kan. 838, 8 P.2d 305 (1932); *Boston Safe Deposit & Trust Co. v. Thomas*, 59 Kan. 470, 53 P. 472 (1898); *St. Paul Fire & Marine Ins. Co. v. Upton*, 2 N.D. 229, 50 N.W. 702 (1891). It is interesting to note that in *Stoddart*, the Kansas court relied heavily on *Asher v. Union Ins. Soc.*, 177 Ga. 662, 170 S.E. 786 (1933), which was overruled on review.

⁴⁵ See *Lupke-Rice Ass'n v. Cessna Fin. Corp.*, No. 526-62B (Ind. Super. Ct. 1979); ANDERSON *supra* note 2, § 31:152-165. See *Annot.* 56 A.L.R. 679 (1928).

gee's obligation to pay past-due premiums. Some policies specifically state that the obligation is dependent upon the demand of the "company." Certainly when the agent advances the premium, he has very little to rely upon under this policy form, because he is not the "company."⁴⁶

CONFISCATION OR SEIZURE

In a recent case, *Lakewood Bank & Trust Co. v. Security Insurance Co. of Hartford*,⁴⁷ an aircraft was delivered to a third party for the purpose of a sales demonstration. Without the knowledge or consent of the owner, the aircraft was flown to Peru and confiscated.⁴⁸ The insurer denied coverage to the mortgagor and to the mortgagee based upon the underlying policy exclusion which stated that no coverage is afforded with respect to physical damage: "to a loss or damage due to conversion, embezzlement or secretion by any person in possession of the aircraft . . . nor for any loss or damage during or resulting therefrom"⁴⁹ The mortgagee argued that the above provision was inconsistent with the BOW, which provided that: "the insurance afforded by the policy shall not be invalidated as regards the interests of the lienholder by any act or neglect of the insured"⁵⁰ The court found that the aircraft was converted by the third party while it was in his possession under a bailment, and that there was no ambiguity between the underlying policy and the BOW.⁵¹ Instead, the court found that the clear language of the BOW continues protection where, "but for" the mortgagor's action, the policy would have provided coverage, and does not create protection in a situation where "but for" the mortgagor's action, there would have been no loss.⁵² It is important to recog-

⁴⁶ Exceptions are AVEMCO Insurance Company and National Aviation Underwriters.

⁴⁷ 1982 FIRE & CASUALTY CAS. 414 (CCH) (N.D. Tex. 1981).

⁴⁸ *Id.* at 415.

⁴⁹ *Id.* at 416.

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.* at 417. See also *General Elec. Credit Corp. v. Ins. Co. of Pennsylvania*, 16 Av. Cas. 17,743 (N.D. Tex. 1980); *AVEMCO Ins. Co. v. Jefferson Bank & Trust Co.*, 16

nize, however, that the main policy and the BOW contained exclusionary language relative to "conversions." Consequently, once there is a finding that the aircraft has been converted, there is no coverage under either policy for the loss.

In *Security Insurance Co. of Hartford v. Commercial Credit Equipment Corp.*⁵³ and *American National Bank & Trust Co. v. Young*,⁵⁴ a different result was reached. *Security* involved an aircraft flown to Colombia by the mortgagor's pilot and detained there by the Colombian government. The insurer denied coverage to the mortgagor and mortgagee, and maintained that the policy insured direct physical loss and disappearance or damage to the aircraft, and did not insure against detention by a governmental authority.⁵⁵ The insurer also relied upon the policy exclusions relating to war, insurrection and the like.⁵⁶ The mortgagee relied upon the BOW language which provided that the insurance shall not be invalidated as to the mortgagee by any act or neglect of the mortgagor.⁵⁷ The court found that the BOW created a sepa-

Av. Cas. 17,242 (Mo. Ct. App. 1980).

⁵³ 399 So. 2d 31 (Fla. Dist. Ct. App. 1981).

⁵⁴ *American Nat'l Bank & Trust Co. v. Young*, No. 438983, slip op. (Minn. Ramsey County Dist. Ct. Jan. 28, 1982).

⁵⁵ 399 So. 2d at 32.

⁵⁶ *Id.* at 33. The policy in *Security* provided:

Exclusions. This policy does not apply and no coverage is afforded: . . . 6. To any loss, or damage or legal liability directly or indirectly occasioned by, happening through or in consequence of war, invasion, acts of foreign enemies, hostilities (whether war be declared or not), civil war, rebellion, revolution, insurrection, military or usurped power or confiscation or nationalization or requisition or destruction of or damage to property by or under the order of any government or public or local authority. . . . 17. To any loss or damage arising from war, invasion, civil war, revolution, rebellion, insurrection or warlike [sic] operations, whether there be a declaration or war or not, or capture, seizure, arrest, restraint, or detention, or the consequences thereof or of any attempt thereat, or any taking of the property insured, or damage to or destruction thereof, by any government or governmental authority or agent, whether secret or otherwise or by any military, naval or usurped power, whether any of the foregoing be done by way of confiscation, requisition or otherwise and whether in time of peace or war, and whether lawful or unlawful.

Id.

⁵⁷ *Id.* The policy in *Security* provided:

This insurance as to the interest of the said lienholder shall not be

rate and distinct contract between the mortgagee and insurer and contained its own exclusions. The court held that, when the exclusions in a policy conflict with the specific provisions of the BOW, the language in the BOW prevails.⁵⁸

In *American National Bank*, under a similar set of circumstances, the insurer argued that the seizure of the aircraft was specifically excluded from coverage by the main policy exclusions which provided that:

This policy does not apply . . . (h) Under Coverages A, B, and C, to occurrences, accidents or losses (1) during or in connection with a flight involving trafficking [sic] in narcotics, drugs or hallucinogens . . . , or (2) due to (a) capture, seizure . . . , or the consequences thereof or any attempt thereat, or any taking of the aircraft or any loss or damage thereof by any government or governmental authority or agent. . . .⁵⁹

and further that the BOW itself contained a "savings clause" (my language, not that of the insurer) that stated:

Nothing herein contained shall be held to vary, waive, alter or extend any of the terms, conditions, agreements, or warranties of the below mentioned policy, *other than as above stated*.⁶⁰

The court, in its decision, reviewed the fundamental rules of construction for interpreting an insurance contract and provided a brief history of the standard mortgage clause. Based on its analysis, the court found coverage for the mortgagee under the BOW. The court further concluded that the provision in the BOW clearly and plainly stated that the interests

invalidated by any act or neglect of the lessee, mortgagor or owner of the within-described aircraft nor by any change in the title or ownership of the property; provided, however, that the wrongful conversion, embezzlement or secretion by purchaser, mortgagor or lessee in possession under a mortgage, conditional sale or lease agreement of the aircraft insured is not covered under this policy, unless specifically insured against and premium paid therefor, provided, also, that in case the lessee, mortgagor or owner shall neglect to pay any premium due under such policy, the lienholder shall, on demand, pay the same.

Id. at 33-34.

⁵⁸ *Id.* at 34.

⁵⁹ *American Nat'l Bank & Trust Co. v. Young*, No. 438983, slip op. at 3 (Minn. Ramsey County Dist. Ct. Jan. 28, 1982).

⁶⁰ *Id.* at 5 (emphasis supplied by the court).

of the mortgagee " 'shall not be invalidated by any act or neglect' of [the mortgagor] 'except that of conversion, embezzlement or secretion.' " ⁶¹ The BOW "savings clause" was held to be merely a statement of the rules of construction, when the provisions of the main policy conflict with the BOW. ⁶²

The decisions in *Lakewood*, *Security* and *American National Bank* appear to be inconsistent. However, a close reading reveals that there is no actual inconsistency. In *Lakewood*, the court reached its decision based upon the finding that the aircraft had been converted. ⁶³ This position is consistent with both the main policy and the BOW, because both provide exclusionary language for conversion, embezzlement or secretion. On the other hand, in *Security* and *American National Bank*, the courts did not find a conversion and therefore were left to consider the applicability of the main policy exclusions to the BOW. ⁶⁴ In both *Security* and *American National Bank* the court found that the main policy exclusions conflicted with the BOW language concerning invalidation of the coverage as to the mortgagee by any act or neglect of the mortgagor. ⁶⁵

TERRITORIAL LIMITS

Any aircraft insurance policy will always include a section dealing with or restricting coverage to a specified territorial area. These limits may be modified or extended by endorsement; however, any loss or occurrence that arises outside the specified area will be excluded from coverage. This territorial limitation creates two interesting questions: (1) What falls within the policy's territorial limits? and (2) Whether a breach of the policy's territorial limits will void coverage under the BOW?

In order to void coverage, an insurer must establish that the

⁶¹ *Id.*

⁶² *Id.*

⁶³ See *supra* notes 47-54 and accompanying text.

⁶⁴ 399 So. 2d at 32; *American Nat'l Bank & Trust Co. v. Young*, No. 438983, slip op. at 5 (Minn. Ramsey County Dist. Ct. Jan. 28, 1982).

⁶⁵ 399 So. 2d at 32; *American Nat'l Bank & Trust Co. v. Young*, No. 438983, slip op. at 5 (Minn. Ramsey County Dist. Ct. Jan. 28, 1982).

words used in a policy not only may be construed according to the company's interpretation, but that the interpretation is the *only* one that may be fairly placed on those words.⁶⁶

The issue of what effect a policy's territorial limitations have on coverage under the BOW was addressed in *Americas Aviation v. Marine Insurance Co.*,⁶⁷ a case in which an aircraft was damaged outside the territorial limits set by the policy and the mortgagee sought recovery for the loss.⁶⁸ The court found that the policy's territorial limitations were in conflict with the BOW and therefore the BOW mandated coverage.⁶⁹

CANCELLATION

Most BOW forms require that, in the event the insurer cancels the policy and gives notice to the mortgagor, he is likewise obligated to give notice to the mortgagee.⁷⁰ When the insurer is cancelling the policy for nonpayment of the premium, both the main policy and the BOW require that notice be given to both the mortgagor and mortgagee. The policy should specify what type of cancellation notice may be given. In the event the insurer gives notice of a potential future cancellation to the mortgagee, if the premium has not been paid, such notice may be insufficient to cancel the mortgagee's coverage under the BOW. The key to cancellation treatment is

⁶⁶ *Vargas v. Ins. Co. of N. Am.*, 16 Av. Cas. 17,508 (2d Cir. 1981); ANDERSON, *supra* note 2, § 37:1476.

⁶⁷ 229 So. 2d 314 (Fla. Dist. Ct. App. 1969).

⁶⁸ *Id.* at 316.

⁶⁹ *Id.* It is apparent, for example, that in *Security Ins. Co. of Hartford*, 339 So. 2d 31 (Fla. Dist. Ct. App. 1981), the Colombian detention was outside the territorial limits of the policy, although this issue was not addressed by the Florida court. The court's silence and its ultimate decision indicate that the court found the territorial limitations provisions of the underlying policy inapplicable for purposes of voiding coverage as to the mortgagee.

It is my opinion that the courts in *Lakewood Bank and Trust Co.*, 1982 FIRE & CASUALTY CAS. 414 (CCH) (N.D. Tex. 1981) and *General Electric Credit Corp.*, 16 Av. Cas. 17,743 (N.D. Tex. 1980) were confronted with the applicability of territorial limitations to coverage under the BOW. However, neither court directly addressed this issue.

⁷⁰ See *supra* notes 10, 17 and accompanying text.

the existence of two separate insurance policies.⁷¹ Cancellation of one does not necessarily cancel the other. Specific written notice of the BOW cancellation should be given if that is what is intended. Otherwise the BOW coverage may survive cancellation of the underlying policy.

Another issue, while not addressed by any court, is the effect of cancellation of the underlying policy by the mortgagor. Does this likewise cancel the BOW, and if it does, should the mortgagee receive notice of cancellation? As a general rule, when a mortgagor cancels his insurance policy, the insurer treats this as a cancellation of the BOW. The aviation managers and underwriting insurance company involved, however, may or may not give notice of that cancellation to the mortgagee. Because the mortgagor and mortgagee theoretically have separate policies of insurance, reliance upon the mortgagor's cancellation for purposes of cancelling the BOW, particularly where notice is not provided to the mortgagee, involves significant risk. Regardless of what the policy may say about notice, the insurer is taking a chance by failing to give notice to the mortgagee.

WHEN IS THERE A "LOSS" UNDER THE BOW?

Another troublesome area is the determination of when a "loss" occurs under the BOW, because the BOW does not define "loss". Consequently, it is necessary to interpret the gray area between two policies, the main policy and the BOW, to find a definition. Under the main policy, "loss" is discussed in the insuring agreement and in that context it occurs when there is a "direct physical loss or direct physical damage."⁷² The term, however, is not defined within the definitional section of the main policy, nor is it fully explained in the policy conditions.

This problem is compounded in the BOW because "loss" is

⁷¹ *American Mercury Ins. Co. v. Inland-Western Fire Ins. Co.*, 6 Ariz. App. 409, 433 P.2d 60 (1967); *Employers Fire Ins. Co. v. Pennsylvania Millers Mutual Ins. Co.*, 116 Ga. App. 433, 157 S.E.2d 807 (1967); 11 APPLEMAN *supra* note 2, § 3401.

⁷² See *supra* notes 6, 10 and accompanying text.

not defined and it is used singularly, without clarification.⁷³ The lack of a definition of "loss" in the BOW makes it unclear as to whether there must be a direct physical loss under the BOW for the mortgagee to recover. Another problem area results from the fact that the BOW limits the amount payable to the mortgagee to the amounts remaining due after the mortgagee "*has used all reasonable means to collect amounts due*" from the mortgagor.⁷⁴ Consequently, the parties are left to determine what "all reasonable means to collect" actually requires, what losses may be covered, and when that loss has occurred.

The *policies* arguably indicate that the mortgagee does not have a "loss" until such time as: (1) coverage has been successfully denied to the mortgagor; (2) the mortgagee has taken possession of the aircraft and sold same; (3) the mortgagee has applied the sale proceeds to the debt; and (4) the mortgagee has pursued the mortgagor for any sums remaining due. When all four criteria have been met the mortgagee has established a direct measurable loss. From the mortgagee's point of view, however, a "loss" has been sustained when: (1) there is a default under its contract with the mortgagor; (2) the aircraft value is less than the amount due under the contract; and (3) the mortgagor has failed to satisfy its obligation in full.

While policy language problems add to the confusion surrounding what constitutes a loss under the BOW, there are administrative and philosophical differences as to what constitutes a "loss" and what may constitute "reasonable means to collect" on the part of the mortgagee. To resolve these differences, the courts may be required to weigh the respective obligations of the parties involved. While there are not any cases directly on point, two cases appear to hold that the mortgagee need not sustain a direct measurable loss to recover under the BOW.

In *Cessna Finance Corporation v. Ranger Insurance Co.*,⁷⁵ it was held that the mortgagee does not have to repossess and

⁷³ *Id.*

⁷⁴ *Id.*

⁷⁵ 15 Av. Cas. 17,309 (D. Kan. 1979).

deliver possession of an aircraft to the insurer as a condition to payment under the BOW.⁷⁶ While there was never a question as to whether the aircraft was "physically damaged," the court, by not requiring a repossession to sustain recovery under the BOW, implies that the mortgagee under the BOW does not have to incur a direct measurable loss. The impairment of the mortgagee's position may be sufficient to establish a recovery.

In *Security Insurance Co. v. Commercial Credit Equipment*,⁷⁷ the court, noting that the BOW uses the term "loss" not "direct physical loss," concluded that "[w]hen a policy provision remains undefined, common everyday usage determines its meaning."⁷⁸ Consequently, the court found no requirement under the BOW that there be a direct physical loss, and the confiscation of the aircraft was a loss covered under the BOW.⁷⁹

MANUFACTURER FINANCING AND THE BOW

What happens when a manufacturer provides financing for an aircraft and is named in a loss payable clause or BOW? Does this have any impact upon a loss that may be the result of a product defect, and if so, what, if any, right of subrogation may the insurer have as against the manufacturer?

This issue was decided in *Allegheny Airlines, Inc. v. General Motors Corp.*⁸⁰ In *Allegheny*, the airline (Allegheny) purchased an aircraft which was financed by General Motors (GM).⁸¹ The Allegheny policy contained a BOW in favor of GM.⁸² The aircraft crashed and was destroyed, allegedly as a result of GM's negligent design and manufacture. The insurer paid the claim and thereafter, through the policy subrogation provisions, attempted to recover against GM.⁸³ The court

⁷⁶ *Id.*

⁷⁷ 399 So. 2d 31 (Fla. Dist. Ct. App. 1981).

⁷⁸ *Id.* at 34.

⁷⁹ *Id.*

⁸⁰ 11 Av. Cas. 17,391 (N.Y. 1969).

⁸¹ *Id.*

⁸² *Id.*

⁸³ *Id.*

found that GM was a named insured under the policy and the insurer was barred from recovery.⁸⁴

Textron, Inc., through its Bell Helicopter Division, has likewise been successful in having product coverage extended to situations in which they are named on the mortgagor's insurance policy and have manufactured, sold and financed the helicopter.⁸⁵ The concept was extended to include lease situations in *BOW Helicopters, Ltd. v. Avco Lycoming Engine Group, Stratford Division*.⁸⁶ The main rationale for the extension of coverage is that the insurer is precluded from recovering from its own insureds for the losses it insures against. While this appears to be harsh, because the insurer probably had no present intent to assume product coverage, the manufacturer's argument and position is simple: it is the "insured" under the insurance policy.

The good news is that not all aircraft manufacturers sell direct or directly finance aircraft purchases. The bad news is that many of the heavy iron manufacturers do sell direct and finance. The specific entity providing the financing, however, may be a subsidiary of the manufacturer. Consequently, the insurer may not be providing product coverage, because the entity providing the financing is different from the manufacturer and, as a result, the manufacturer itself may not be a "named insured". In any event, the insurer is unquestionably going to have a great deal of difficulty in denying product coverage where the manufacturer is the named insured in the BOW and directly sells and finances the product.

SUBROGATION

The BOW presents some rather unique subrogation problems. All of the various policy forms provide for subroga-

⁸⁴ *Id.* at 17,392.

⁸⁵ See, e.g., *Croman Corp. v. Textron, Inc.*, No. 78-396, slip op. (D. Or. May 20, 1980) (order denying defendant's motion for partial summary judgment); *Corvallis Aero Service, Inc. v. Textron, Inc.*, No. 80-6249-E, slip op. (D. Or. April, 22, 1981) (order granting defendant's motion for partial summary judgment); *BOW Helicopters, Ltd. v. Avco Lycoming Engine Group, Stratford Division*, slip op. (Alta. Ct. App. June 15, 1981) (order dismissing appeal).

⁸⁶ No. 978 C.A. Alberta.

tion and, in some instances, for an assignment of the mortgagee's rights as against the mortgagor. When the insurer pays the mortgagee for a loss under the BOW and that amount is less than the total indebtedness, in order for the insurer to be allowed subrogation to the mortgagee's rights, the insurer must prove that its obligation to the mortgagor was void. Merely establishing that recovery under the underlying policy was suspended by the mortgagor, or that the mortgagor obtained additional insurance, is not sufficient.⁸⁷

The court, in *MFA Mutual Insurance Co. v. Huddleston*,⁸⁸ found that the acquisition of additional insurance by the mortgagor did not increase the possibility of hazards. Therefore, the contemplation of the parties and payment by the insurer under the BOW was simply a discharge of the insurer's obligation to the mortgagee. The policy was not actually "voided" but merely suspended due to a technicality.⁸⁹ When the insurer does make a payment to the mortgagee pursuant to the BOW, the insurer's right of subrogation is based upon the insurance contract itself and any ambiguity in the language of the policy should be construed and interpreted against the insurer.⁹⁰ Moreover, most courts have found that the subrogation provision of the BOW does not impair the mortgagee's rights to collect all of his remaining debt. The interests of the insurer in this instance are subrogated to those of the mortgagee, because it is only a fortuitous circumstance that relieves the insurer of an absolute liability, and there is no reason, absent specific language, to further benefit the insurer.⁹¹ The insurance proceeds paid to the mortgagee pursuant to the BOW will not operate to reduce or extinguish the mortgage debt or to discharge the mortgage, but only operate

⁸⁷ *MFA Mutual Ins. Co. v. Huddleston*, 459 S.W.2d 104 (Mo. Ct. App. 1970).

⁸⁸ 459 S.W.2d 104 (Mo. Ct. App. 1970).

⁸⁹ *Id.* at 108.

⁹⁰ *Lervold v. Republic Mut. Fire Ins. Co.*, 142 Kan. 43, 45 P.2d 839 (1935).

⁹¹ *Id.* at 49, 45 P.2d at 843. See *Nat'l Bank of Or. v. American Home Assurance Co.*, 347 F. Supp. 311 (D. Or. 1972); *Savings Bank v. Schancupp*, 108 Conn. 588, 144 A. 36 (1928); *Quincy Mut. Fire Ins. Co. v. Jones*, 486 S.W. 2d 126 (Tex. Civ. App.—Dallas 1972, no writ); *National Ben Franklin Ins. Co. v. Praetorians*, 67 S.W.2d 333 (Tex. Civ. App. — El Paso 1934, writ ref'd).

to satisfy, *pro tanto*, the mortgagee's claim. The mortgage is left in full force against the mortgagor, with no right on the mortgagor's part to claim a reduction in the debt as a result of the insurer's payment to the mortgagee.⁹² Cases have held that the insurer may gain additional rights in the event he pays the mortgagee in full. The insurer takes a full assignment of the rights of the mortgagee, and the insurer gets the right to demand payment of the mortgage and the right to foreclose if the debt remains unpaid.⁹³

The issue of subrogation, with regard to the aircraft BOW, is complicated further by the fact that the BOW itself seems to make no provision for a partial loss. It provides for payment on a stated value basis with the insurer obtaining a full assignment.⁹⁴ The provisions dealing with a partial loss are found within the underlying policy conditions and the applicable policy definitions. It seems clear, therefore, that because the BOW specifically addresses the issue of payment of a loss, any loss should be paid in accordance with the provisions of the BOW. To treat the payment any other way would be to give to the insurer the benefit of construing an ambiguity in the policy in its favor.

As a practical matter, this problem may not be significant because most mortgagees are simply interested in being made whole. Consequently, they may be willing to recover for a loss on a partial basis. In the event of partial payment, however, there will be an inherent problem with regard to the insurer's rights of subrogation and to any potential assignment. When an insurer voluntarily makes a payment outside the BOW's specific terms, it is my opinion that the insurer is not entitled to any benefits that the mortgagee may have as against the mortgagor.⁹⁵

⁹² *Savings Bank v. Schancupp*, 108 Conn. 588, 144 A. 36 (1928); *Quincy Mut. Fire Ins. Co. v. Jones*, 486 S.W.2d 126 (Tex. Civ. App.—Dallas 1972, no writ).

⁹³ *National Ben Franklin Ins. Co. v. Praetorians*, 67 S.W.2d 333 (Tex. Civ. App.—El Paso 1934, writ ref'd).

⁹⁴ See *supra* note 6 and accompanying text.

⁹⁵ This position, I feel, is consistent with the *Lervold*, *Savings Bank* and *National Bank of Oregon* decisions discussed above. See *supra* notes 90-91 and accompanying text.

CONCLUSION

Because of the highly mobile nature of aircraft and the unique requirements of airworthiness certification, as well as pilot licensing, the aircraft BOW is more complex than the BOW found in a standard fire insurance policy. As many of the cases illustrate, the direct relationship of the aircraft BOW to the underlying policy terms and conditions is not always clear. This uncertainty makes it difficult to predict with any degree of accuracy what acts or neglect by the mortgagor may give rise to coverage for the mortgagee under the BOW.

Without question, the BOW is ripe for litigation. The overall problem is compounded by: (1) inherent differences in the interests of the insurer and the mortgagee; (2) the basic underwriting intent and the fact that it is not clearly and specifically encompassed within the BOW; (3) the lack of uniformity in the more than twenty different forms of the BOW; (4) the issuance of some BOW's by direct writers, some by aviation managers, and some by lending institutions; (5) the fact that many BOW forms are produced by assembling and grafting various policy phrases and clauses together; and (6) the inherent difficulty in determining what the exact relationship may be between the main policy and the BOW.

All of these problem areas may eventually be resolved through litigation. Litigation, however, is an unnecessary and costly resolution to the problem, even if only legal fees are considered. The better approach would be to draft a BOW with clear and concise policy language. While this is an easy statement to make, the problems of accomplishing the task without changing the manner in which we look at the BOW itself are numerous. Whether a clarification of the relationship between the main policy and the BOW is attempted or the BOW is made truly a separate policy, the drafter will have to put all his legal faculties to work.

A clear and concise BOW will not be accomplished unless there is some cooperation between the insurers and lenders, both of whom have substantial interests to protect, and both of whom have different philosophical understandings of the BOW. The insurer believes that the BOW cannot extend cov-

erage where there was *NO* coverage under the main policy, in the first instance. The mortgagee, on the other hand, believes that the BOW extends coverage where the main policy may be voided by any act of the mortgagor. If cooperation can be achieved, however, it will enable all parties involved to understand the coverage extended and, further, it should provide the insurer with a better mechanism for rating the coverage and risks involved. It will also give an opportunity to the mortgagor to protect his interests in some other fashion, if that is necessary.